Because learning changes everything.®

Chapter 3

The Organizational Environment and Culture

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Learning Objectives

LO 1 Describe the five elements of an organization's macroenvironment.

LO 2 Explain the five components of an organization's competitive environment.

LO 3 Learn how managers stay on top of changes in the external environment.

LO 4 Summarize how managers interact with the external environment.

LO 5 Discuss how to use organizational cultures to overcome challenges in the external environment.

LO 6 Discuss how an organization's culture and climate affect its response to its external environment.

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Open Systems

Organizations are **open systems** that affect and are affected by their environments and other systems.

- *Inputs* are goods and services that organizations take in and use to create products or services.
- *Outputs* are the products and services organizations create.

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External Environment

The **external environment** is more than an organization's customers, partnerships or suppliers.

- All relevant forces outside a firm's boundaries.

Gordon Logan, founder of Sport Clips, created the successful business after conducting market research that showing little competition in the men's haircut market.

Wendy Yang/KRT/Newscom

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The Macroenvironment

Macroenvironment

- The general environment: includes governments, economic conditions, and other fundamental factors that generally affect all organizations.
- May be uncontrollable.

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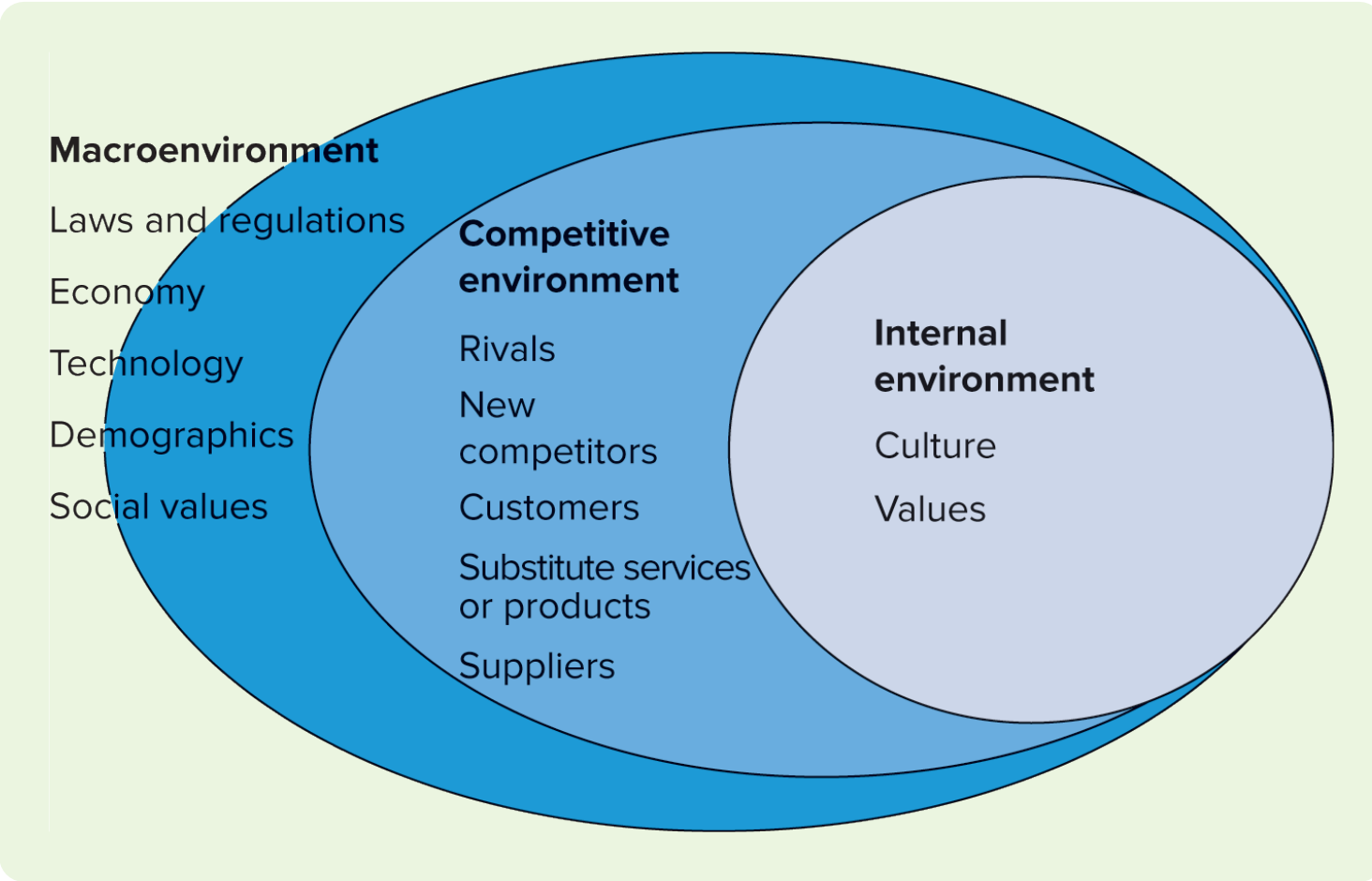
Exhibit 3.1: Environments



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Laws and Regulations Protect and Restrain Organizations

United States Regulators

- Environmental Protection Agency (epa.gov).
- Federal Communications Commission (fcc.gov).
- Federal Reserve System (federalreserve.gov).
- Food and Drug Administration (fda.gov).
- National Labor Relations Board (nlrb.gov).
- Nuclear Regulatory Commission (nrc.gov).
- Occupational Safety and Health Administration (osha.gov).

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The Economy Affects Managers and Organizations

Economic Factors

- Interest and inflation rates.
- Unemployment rates.
- Stock markets.

The Russian invasion of Ukraine immediately disrupted global energy supply chains and forced many Western nations to reevaluate their reliance on Russian oil and fossil fuels more broadly.

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Technology Is Changing Every Business Function

Technological Advances

- New industries, new markets, new products.
- Provide more efficient ways to manage and communicate.

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Demographics Describe Your Employees and Customers

Demographics

Statistical characteristics of a group or population such as age, gender, and education level.

Managers must consider workforce demographics:

- Population growth.
- Education and skill levels of the workforce.
- Immigration.
- Diverse customer base needs.
- Age.

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Social Values Shape Attitudes Toward Your Company and Its Products

Societal Trends

- Have major implications for management of the labor force, corporate social actions, and strategic decisions about products and markets.
- Companies introducing more supportive policies for working families and for work-life balance.
- Prominent issues related to sustainability.
- Companies' responses to social issues may affect their reputation.

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The Competitive Environment

Competitive Environment

The immediate environment surrounding a firm; includes suppliers, customers, rivals, and the like.

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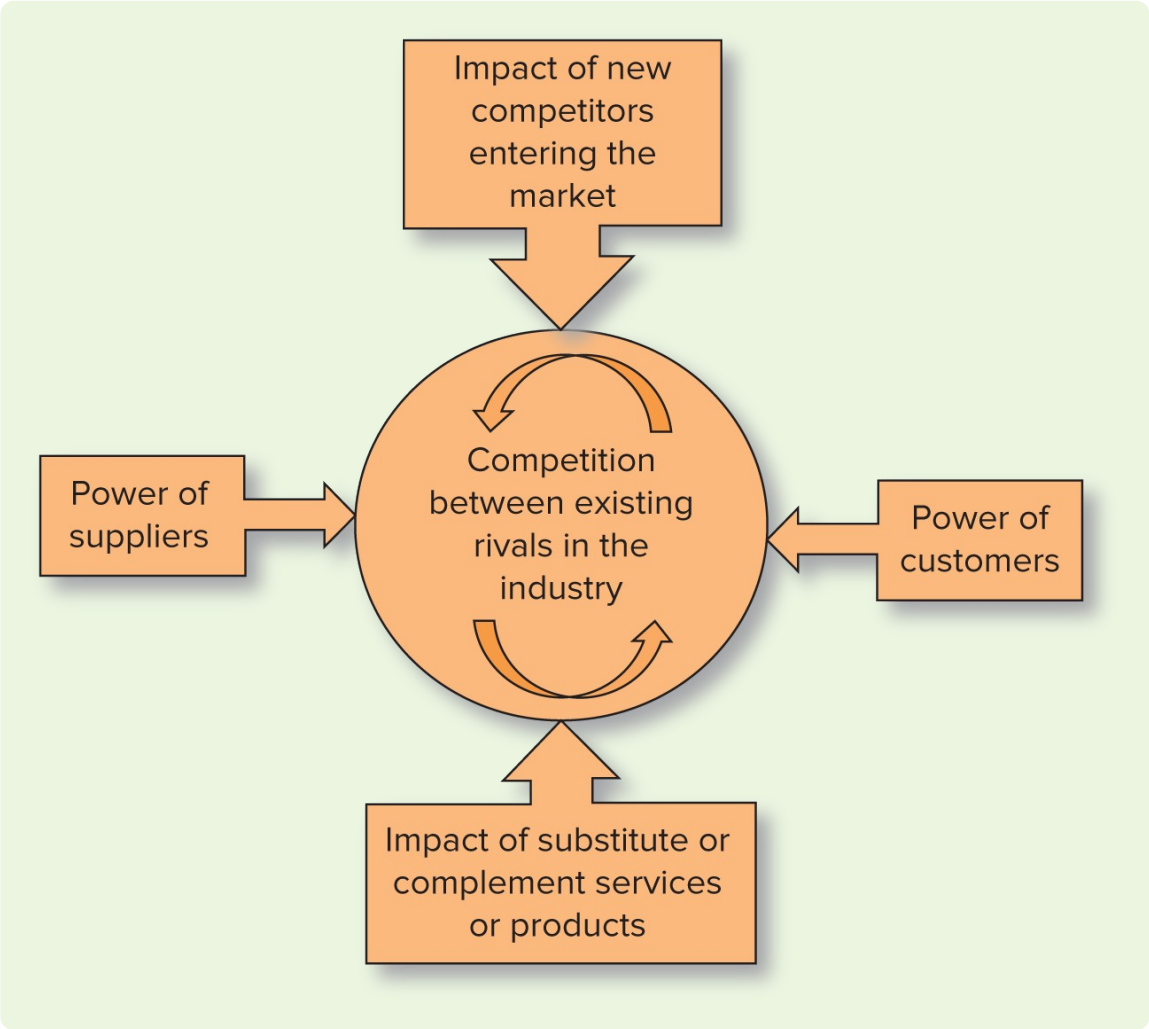
Exhibit 3.2: Porter's Five Forces


Impact of new competitors entering the market
Power of suppliers
Competition between existing rivals in the industry
Power of customers
Impact of substitute or complement services or products

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Source: Adapted from M. E. Porter, "The Five Competitive Forces That Shape Strategy," *Harvard Business Review*, www.hbr.org (January 2008), pp. 78–93

Rivals Can Be Domestic or Global

Identify the Competition

- Small domestic firms.
- Strong regional competitors.
- Big new domestic companies exploring new markets.
- Global firms.
- Newer ventures.

Analyze How They Compete

- Competitors use tactics such as price reductions, new-product introductions, and advertising campaigns to gain advantage over their rivals.

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New Entrants Appear When Barriers to Entry Are Low

Barriers to Entry

Conditions that prevent new companies from entering an industry.

Include:

- Government policy.
- Capital requirements.
- Brand identification.
- Cost disadvantages.
- Distribution channels.

If you are a racing fan or use the products she endorses, you'll recognize Danica Patrick. Who are your most and least favorite athlete/endorsers, and what makes them so?

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Customers Determine Your Success

Customers

- **Final consumers** are those who purchase products in their finished form.
- **Intermediate consumers** are customers who purchase raw materials or wholesale products before selling them to final customers (B2B companies).
- Customer service means giving customers what they want or need, the way they want it, the first time.

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Competitors' Products Can Complement or Substitute for Yours

Substitutes

- A potential threat; customers use it as an alternative, buying less of one kind of product but more of another.
- Firms can develop substitutes with technological advances and economic efficiencies.

Complements

- A potential opportunity; customers buy more of a given product if they also demand more of the complementary product.

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Exhibit 3.3: Potential Substitutes and Complements

If the Product is…	The Substitute Might Be…
Chipotle Burrito Bowl	Chick-fil-A meal
Apple Watch	Samsung Galaxy Watch
Ford F-150 truck	Chevy Silverado truck
Evernote	Dropbox

If the Product is…	The Complement Might Be…
HTC Vive virtual reality headset	Eagle Flight game
Amazon streaming video	Strawberry Twizzlers
Health club membership	Workout clothes
Apartment rental	IKEA furniture

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Suppliers Provide Your Resources

Suppliers

- Provide resources needed for production: people, raw materials, information, and financial capital.
- **Switching costs** are fixed costs buyers face when they change suppliers.
- **Supply chain management** is the managing of the network of facilities and people that obtain materials from outside the organization, transform them into products, and distribute them to customers.
- Choosing right supplier is an important strategic decision.

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Keeping Up with Changes in the Environment

Environmental Uncertainty

When management lacks information to understand or predict the future.

Uncertainty arises from:

- Complexity—the number of issues a manager must attend to and the degree to which they are interconnected.
- Dynamism—the frequency of significant change occurring within the industry.

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Environmental Scanning Keeps You Aware

Environmental Scanning

- Searching for and sorting through information about the environment.

Competitive Intelligence

- Information that helps managers determine how best to manage in the competitive environment.
- Environments can be attractive (competitive advantage) or unattractive (competitive disadvantage).

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Exhibit 3.4: Attractive and Unattractive Environments

Environmental Factor	Attractive	Unattractive
Competitors	Few; high industry growth; unequal size differentiated.	Many; low industry growth; equal size; commodity.
Threat of entry	Low threat; many barriers.	High threat; few entry barriers.
Substitutes	Few.	Many.
Suppliers	Many; low bargaining power.	Few; high bargaining power.
Customers	Many; low bargaining power.	Few; high bargaining power.

Sources: Adapted from S. Ghoshal, "Building Effective Intelligence Systems for Competitive Advantage," *Sloan Management Review* 28, no. 1 (Fall 1986), pp. 49–58; and K. D. Cory, "Can Competitive Intelligence Lead to a Sustainable Competitive Advantage?" *Competitive Intelligence Review* 7, no. 3 (Fall 1996), pp. 45–55.

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Forecasting Predicts Your Future Environment

Forecasting

Method for predicting how variables will change the future.

When using forecasts:

- Use multiple forecasts.
- Remember accuracy decreases as you go further into the future.
- Collect data carefully.
- Use simple forecasts.
- Remember that important events can be surprises that sabotage predictions.

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Developing Scenarios Helps You Think About the Future

Scenarios

- A narrative that describes a particular set of future conditions.
- Best-case, worst-case.
- Update regularly to account for relevant new factors.

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Responding to the Environment 1

Effective Responses

- Adapting to the environment.
- Influencing the environment.
- Selecting a new environment.

Adapt to the External Environment

- **Empowerment** shares power with employees at all levels to enhance their contributions to the organization.

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Responding to the Environment 2

Adapting at the Boundaries

- **Buffering** is creating supplies of excess resources in case of unpredictable needs.
- **Smoothing** is leveling normal fluctuations at boundaries of the environment.

Adapting at the Core

- **Flexible processes** allow for adaptation in the technical core to meet varied and changing demands of customers.

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Influence Your Environment

Independent Strategies

Strategies an organization acting on its own uses to change some aspect of the current environment.

- Competitive aggression.
- Competitive pacification.
- Public relations.
- Voluntary action.
- Legal action.
- Political action.

Cooperative Strategies

Strategies used by two or more organizations working together to manage the external environment.

- Contracts.
- Cooptation.
- Coalition.

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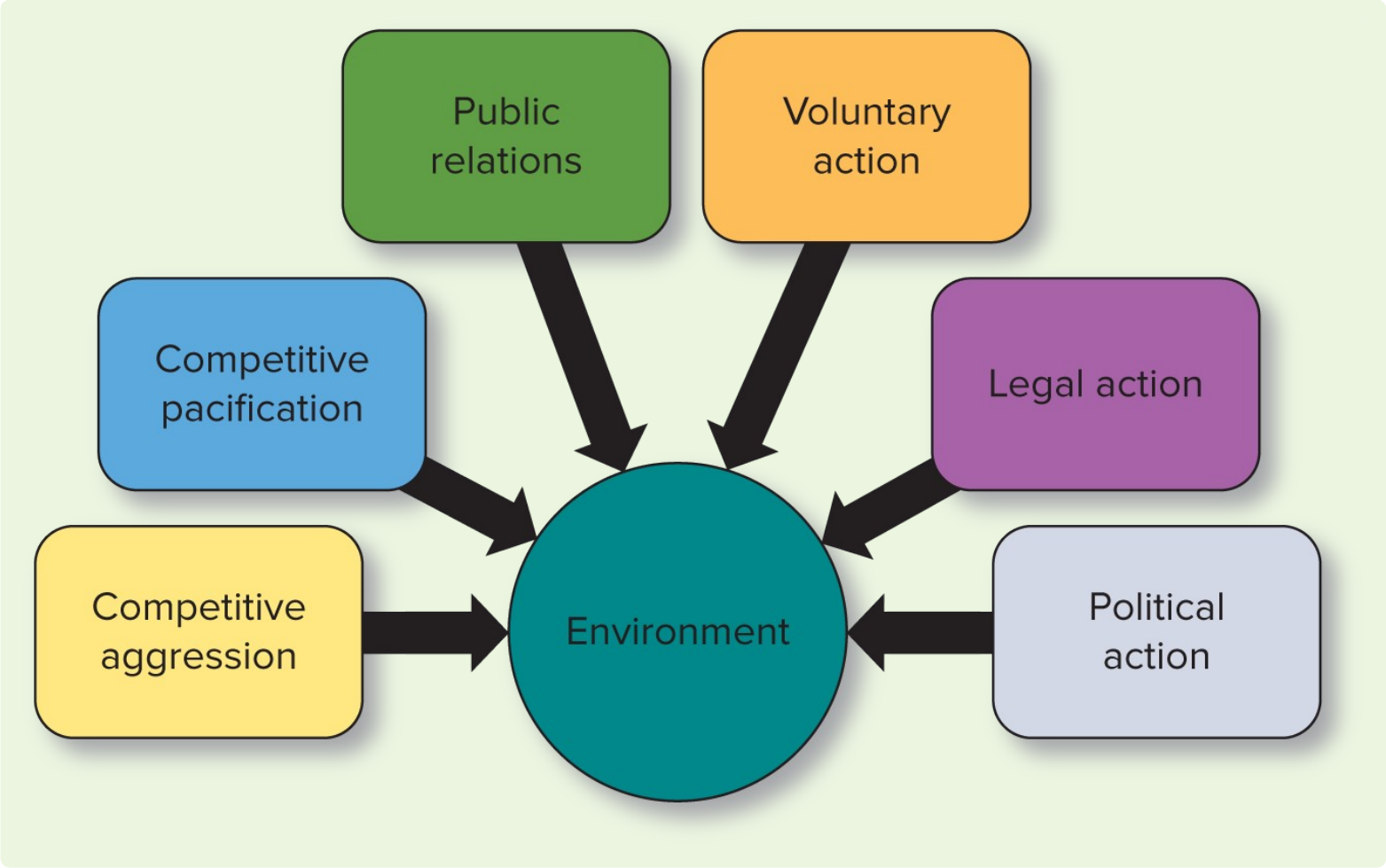
Exhibit 3.5: Examples of Independent Actions



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Change the Boundaries 1

Strategic Maneuvering

- An organization's conscious efforts to change the boundaries of its task environment.
- **Domain selection** is the entrance to a new market or industry with an existing expertise.
- **Diversification** is a firm's investment in a different product, business, or geographic area.

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Change the Boundaries 2

Strategic Maneuvering continued

- **Mergers** happen when companies combine with another.
- **Acquisitions** happen when one firm buys another.
- **Divestiture** is when a firm sells one or more

Alphabet
abc.xyz Alphabet
is for Google
As Sergey and I wrote in the original founders letter 11 years ago, "Google is not a conventional company. We do not intend to become one." more

Alphabet Inc. is an American multinational conglomerate created through a corporate restructuring of Google. Its portfolio encompasses industries such as technology, life sciences, investment capital, and research.

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Change the Boundaries 3

Prospectors

- Continuously change boundaries of their task environment by seeking new products and markets, diversifying and merging, or acquiring new enterprises.

Defenders

- Stay within a stable product domain as a strategic maneuver.

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Three Criteria Help You Choose the Best Approach

1. Managers need to change what matters and is changeable.
2. Managers should use the most appropriate response.
3. Managers should choose responses that offer the most benefit at the lowest cost.

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The Internal Environment: Your Organization's Culture

Environmental Factors Inside the Organization

- Internal culture refers to conditions, routines, and beliefs that both influence and are influenced by the people who work within the organization.

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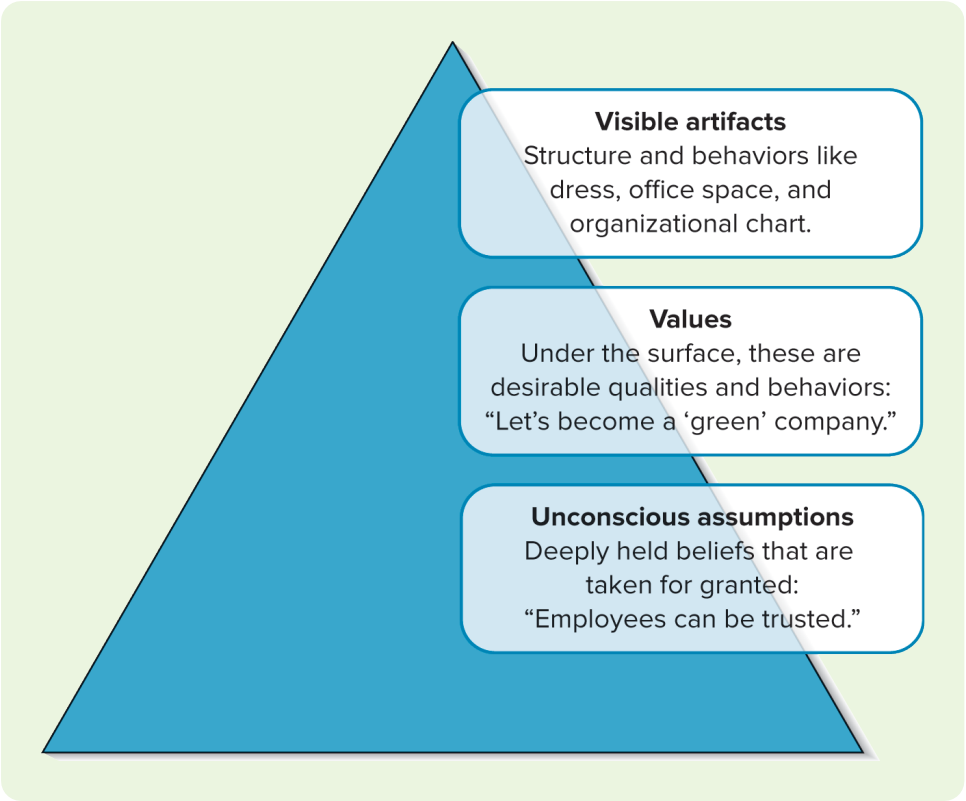
Organizational Culture

Organizational Culture

- Set of important **goals**, practices, and assumptions that members share.
- System of shared values and beliefs.


Visible artifacts
Structure and behaviors like dress, office space, and organizational chart.
Values
Under the surface, these are desirable qualities and behaviors: "Let's become a 'green' company."
Unconscious assumptions
Deeply held beliefs that are taken for granted: "Employees can be trusted."

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Source: Adapted from E. H. Schein, "Coming to a New Awareness of Organizational Culture," Sloan Management Review 25, no. 2 (Winter 1984), pp. 3–16.

Cultures Can Be Strong or Weak 1

Strong Culture

- Everyone understands and believes in the firm's goals, priorities, and practices.
- Can potentially (but not always) be an asset.

Weak Culture

- Different people hold different values, there is confusion about corporate goals, and it is not clear from one day to the next what principles should guide decisions.

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Cultures Can Be Strong or Weak 2

Diagnosing Culture

- Corporate mission statements and official goals.
- Business practices.
- Symbols, rites, and ceremonies.
- The stories people tell.
- Cultural assessments.

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Cultures Can Be Strong or Weak 3

Managing Culture

- Articulate clearly ideals to pursue and values to exhibit.
- Communicate with employees regularly and set the right examples.
- Celebrate and reward those who exemplify the desired culture.

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Group Challenge

Develop a list of substitutes and complements for the following items.

Item	Substitute	Complement
Cornflakes		
Ground beef		
Pencils		
Tablet		
iPad		
Notebook paper		
Hot dogs		
Automobile		

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Chapter Review 1

Five elements of an organization's macroenvironment:

- Laws and regulations, the economy, technology, demographics, and social values.

Five components of an organization's competitive environment:

- Impact of new competitors, power of customers, impact of substitute or complement products, power of suppliers, competition between existing rivals in the industry.

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Chapter Review 2

Keeping up with the environment:

- Environmental scanning, forecasting, scenarios,

Responding to the environment:

- Buffering, smoothing, flexible processes. Independent action and cooperative action. Changing the boundaries.

Organizational culture:

- Goals, practices and assumptions. Shared values and beliefs.

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